

POST ROCK RURAL WATER DISTRICT NO. 1
Ellsworth, Kansas

FINANCIAL STATEMENTS
Years Ended December 31, 2011 and 2010

VONFELDT, BAUER & VONFELDT, CHTD.
Certified Public Accountants
Larned, Kansas 67550

Post Rock Rural Water District No. 1
Financial Statements
Years Ended December 31, 2011 and 2010

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
Post Rock Rural Water District No. 1
Ellsworth, Kansas

We have audited the accompanying balance sheets of Post Rock Rural Water District No. 1, Ellsworth, Kansas, as of December 31, 2011 and 2010, and the related statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Post Rock Rural Water District No. 1, Ellsworth, Kansas, as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 9 to the financial statements, the Company is in default on certain covenants of its loan agreements as of December 31, 2011. These conditions raise substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

VONFELDT, BAUER & VONFELDT, CHARTERED
Certified Public Accountants

February 10, 2012

POST ROCK RURAL WATER DISTRICT NO. 1
ELLSWORTH COUNTY, KANSAS
BALANCE SHEET
December 31, 2011 and 2010

	<u>ASSETS</u>	
	<u>2011</u>	<u>2010</u>
CURRENT ASSETS:		
Cash on Hand	\$ 250.00	\$ 250.00
Cash in Bank	761,346.39	562,764.00
Certificates of Deposit	0.00	5,000.00
Accounts Receivable (Note 3)	2,435.85	27,248.64
Interest Receivable	0.00	11.74
Inventory (Note 7)	115,397.44	137,729.24
Prepaid Expenses	<u>94,203.97</u>	<u>87,131.35</u>
 Total Current Assets	 <u>\$ 973,633.65</u>	 <u>\$ 820,134.97</u>
INVESTMENTS:		
Co-op Stock and Deferred Prorations (Note 2)	<u>\$ 3,664.40</u>	<u>\$ 3,087.97</u>
PROPERTY, PLANT AND EQUIPMENT: (Note 5)		
Land	\$ 25,787.02	\$ 25,787.02
Buildings	195,291.81	195,291.81
Office Furniture & Equipment	392,087.05	355,311.59
Vehicles	244,571.78	231,770.91
Water System	14,057,290.22	14,057,290.22
System Start-Up Costs	1,832,224.10	1,832,224.10
Less - Accumulated Depreciation & Amortization	<u>(8,494,130.03)</u>	<u>(8,109,671.08)</u>
 Net Property, Plant and Equipment	 <u>\$ 8,253,121.95</u>	 <u>\$ 8,588,004.57</u>
 Total Assets	 <u>\$ 9,230,420.00</u>	 <u>\$ 9,411,227.51</u>

The accompanying notes are an integral part of these financial statements

POST ROCK RURAL WATER DISTRICT NO. 1
 ELLSWORTH COUNTY, KANSAS
 BALANCE SHEET
 December 31, 2011 and 2010

	<u>LIABILITIES AND EQUITY</u>	
	<u>2011</u>	<u>2010</u>
CURRENT LIABILITIES:		
Accounts Payable	\$ 25,306.26	\$ 24,207.21
Interest Payable	6,248,744.03	5,846,425.73
Current Portion of Long-Term Debt (Note 9)	<u>3,824,430.82</u>	<u>3,445,360.18</u>
Total Current Liabilities	<u>\$ 10,098,481.11</u>	<u>\$ 9,315,993.12</u>
LONG TERM LIABILITIES:		
Long-Term Debt, less current portion (Note 9)	<u>\$ 1,889,749.66</u>	<u>\$ 2,268,820.30</u>
Total Long-Term Liabilities	<u>\$ 1,889,749.66</u>	<u>\$ 2,268,820.30</u>
Total Liabilities	<u>\$ 11,988,230.77</u>	<u>\$ 11,584,813.42</u>
FUND BALANCES:		
Membership Benefit Units		
Balance, January 1	\$ 1,086,788.61	\$ 1,076,988.61
Sales of Units During Year	<u>16,800.00</u>	<u>9,800.00</u>
Balance, December 31	\$ 1,103,588.61	\$ 1,086,788.61
RETAINED EARNINGS	<u>(3,861,399.38)</u>	<u>(3,260,374.52)</u>
Total Members' Equity	<u>\$ (2,757,810.77)</u>	<u>\$ (2,173,585.91)</u>
Total Liabilities and Equity	<u>\$ 9,230,420.00</u>	<u>\$ 9,411,227.51</u>

The accompanying notes are an integral part of these financial statements

POST ROCK RURAL WATER DISTRICT NO. 1
 ELLSWORTH COUNTY, KANSAS
 STATEMENT OF OPERATIONS
 For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Operating Revenue:		
Facility Revenue	\$ 1,893,942.05	\$ 1,772,600.90
 Total Operating Revenue	 <u>\$ 1,893,942.05</u>	 <u>\$ 1,772,600.90</u>
 Operating Expenses		
Payroll Expenses	\$ 375,218.29	\$ 383,939.85
Employee Benefits	97,685.50	91,232.65
Insurance	51,177.62	55,512.75
Interest	402,318.30	402,706.94
Depreciation	354,398.20	345,998.75
Amortization	45,805.61	45,805.61
Office Expense	26,311.21	23,588.26
Utilities	203,098.15	178,634.39
Rent	11,400.52	62,475.52
Janitor	6,776.51	7,460.50
Meeting Expense	5,310.28	7,174.24
Professional Services	24,327.14	35,823.65
Distribution Expense	618,109.81	255,872.23
Water Purchases	85,088.97	59,362.69
Treatment Plant Expense	213,836.30	141,405.15
Automotive Expense	96,618.04	77,732.53
Dues, Conferences & Schooling	1,800.00	1,260.00
Travel & Entertainment	3,137.53	3,205.78
Shop Expense	2,557.51	2,385.39
Miscellaneous	<u>68.00</u>	<u>215.33</u>
 Total Operating Expenses	 <u>\$ 2,625,043.49</u>	 <u>\$ 2,181,792.21</u>
 Net Income (Loss) from Operations	 <u>\$ (731,101.44)</u>	 <u>\$ (409,191.31)</u>
 Other Income		
Interest Income	\$ 2,734.65	\$ 2,393.11
Miscellaneous Income	15,631.18	18,673.08
Customer Service & Repair	103,872.19	91,167.24
Gain (Loss) on Sale of Equipment	<u>7,838.56</u>	<u>(20,437.69)</u>
 Total Other Income	 <u>\$ 130,076.58</u>	 <u>\$ 91,795.74</u>
 Net Earnings (Loss)	 <u><u>\$ (601,024.86)</u></u>	 <u><u>\$ (317,395.57)</u></u>

The accompanying notes are integral part of these financial statements.

POST ROCK RURAL WATER DISTRICT NO. 1
 ELLSWORTH COUNTY, KANSAS
 STATEMENT OF CHANGES IN RETAINED EARNINGS
 For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Balance, Beginning of Year	\$ (3,260,374.52)	\$ (2,942,978.95)
Net Earnings (Loss)	<u>(601,024.86)</u>	<u>(317,395.57)</u>
Balance, End of Year	<u>\$ (3,861,399.38)</u>	<u>\$ (3,260,374.52)</u>

The accompanying notes are an integral part of these financial statements

POST ROCK RURAL WATER DISTRICT NO. 1
 ELLSWORTH COUNTY, KANSAS
 STATEMENT OF CASH FLOWS
 For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
<u>Cash Flow From Operating Activities</u>		
Net Income	\$ (601,024.86)	\$ (317,395.57)
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation & Amortization	400,203.81	391,804.36
Patronage Dividends Received in the Form of Stock	(576.43)	(599.81)
(Gain) Loss on Sale of Equipment	(7,838.56)	20,437.69
(Increase) Decrease in:		
Trade Receivables	24,812.79	(5,722.47)
Other Receivables & Prepaid Expenses	15,270.92	(19,415.47)
Increase (Decrease) in:		
Trade Accounts Payable	1,099.05	(29,367.88)
Interest Payable	402,318.30	402,318.31
Net Cash Provided By Operating Activities	<u>\$ 234,265.02</u>	<u>\$ 442,059.16</u>
<u>Cash Flow From Investing Activities</u>		
Net (increase) decrease in Certificates of Deposit	\$ 5,000.00	\$ 0.00
Purchases of Equipment and Land	(70,569.46)	(158,270.17)
Proceeds from Sale of Equipment	<u>13,086.83</u>	<u>4,500.00</u>
Net Cash Provided By Investing Activities	<u>\$ (52,482.63)</u>	<u>\$ (153,770.17)</u>
<u>Cash Flow From Financing Activities</u>		
Sale of Membership Benefit Units	\$ 16,800.00	\$ 9,800.00
Debt Reduction	<u>0.00</u>	<u>(19,032.97)</u>
Net Cash Provided By Financing Activities	<u>\$ 16,800.00</u>	<u>\$ (9,232.97)</u>
Net Increase (Decrease) In Cash	\$ 198,582.39	\$ 279,056.02
Cash At Beginning Of Year	<u>563,014.00</u>	<u>283,957.98</u>
Cash At End Of Year	<u><u>\$ 761,596.39</u></u>	<u><u>\$ 563,014.00</u></u>
<u>Supplemental Disclosures</u>		
Interest Paid	<u><u>\$ 0.00</u></u>	<u><u>\$ 388.63</u></u>

The accompanying notes are an integral part of these financial statements

POST ROCK RURAL WATER DISTRICT NO. 1
ELLSWORTH COUNTY, KANSAS
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. The Post Rock Rural Water District was incorporated March 5, 1979. The District was financed by the sale of benefit units to members. A grant related to Phase I Construction for \$5,018,000 was approved from Farmers Home Administration and \$1,421,000 was received during 1984. A grant for \$350,000 was approved from the E.D.A. in 1982. Grants totaling \$3,485,000 were received during 1985. Grants totaling \$184,000 were received during 1986. A grant of \$2,900,000 was approved from Farmers Home Administration related to Phase II Construction and related costs. Grants totaling \$1,374,000 were received in 1986. Grants in 1987 amounted to \$1,978,608. Grants received in 1996 for additional construction amounted to \$500,000.
- B. The records of Post Rock Rural Water District No. 1 are reported on the accrual basis of accounting. Revenues are recognized in the accounting period when they become both measurable and available to finance expenditures of the fiscal period. Expenditures are recognized whenever any indebtedness is created.
- C. Investments are valued at cost. See Note 2.
- D. Property, plant and equipment is recorded at cost, (including amounts under capital leases). When individual items are sold or disposed of, the related cost and accumulated depreciation is removed and the resulting gain or loss is included in the results of operations. The straight-line method is used in computing depreciation based on the useful lives of the individual assets (including capital leases). Maintenance and repairs are expensed as incurred.
- E. Inventory consists primarily of equipment and supplies and are stated at the lower of cost (first-in, first-out) or market.
- F. Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from these estimates.
- G. System start-up costs subjected to amortization include legal fees, bond issue fees, easements, engineering fees, capitalized interest and condemnation fees. System start-up costs are being amortized on a straight-line basis over a forty year period.

Note 2 - INVESTMENTS

Investments consist of stock and deferred prorations in the Ellsworth County Co-op. Investments are carried in the financial statements at cost, which approximates fair value.

Note 3 - ACCOUNTS RECEIVABLE

Accounts receivable is comprised of amounts due from benefit users for additional construction costs specifically related to serving that customer.

Note 4 - CASH & CASH EQUIVALENTS

For purposes of the statement of cash flows, the Company considers all highly liquid debt instruments with a maturity of one month or less to be cash equivalents.

Note 5 - PROPERTY, PLANT & EQUIPMENT

A summary of property, plant and equipment at December 31, 2011 and 2010, is as follows:

	<u>2011</u>	<u>2010</u>
Land	\$ 25,787.02	\$ 25,787.02
Buildings	195,291.81	195,291.81
Equipment and vehicles	636,658.83	587,082.50
Water System	<u>15,889,514.32</u>	<u>15,889,514.32</u>
	<u>\$ 16,747,251.98</u>	<u>\$ 16,697,675.65</u>

Depreciation expense for the years ended December 31, 2011 and 2010, was \$354,398.20 and \$345,998.75, respectively. Amortization of Water System Start-Up costs for the years ended December 31, 2011 and 2010, was \$45,805.61 and \$45,805.61, respectively.

Substantially all property, plant & equipment is held as collateral for FHA.

Note 6 - LEASES

The company enters into both cancelable and noncancelable operating leases. The cancelable leases expire annually. Lease and rent expense for the years ended December 31, 2011 and 2010 was \$11,400.52 and \$62,475.52, respectively.

Note 7 - INVENTORY

Inventory is stated at the lower of cost (determined on the first in, first-out basis) or market. Inventories consisted of the following:

	<u>2011</u>	<u>2010</u>
Parts and supplies	<u>\$ 115,397.44</u>	<u>\$ 137,729.24</u>

Note 8 - CONTINGENCIES

As shown in the accompanying financial statements, the Company incurred net losses from operations of \$731,101.44 and \$409,191.31 for the years ended December 31, 2011 and 2010 respectively. The Company's current liabilities exceeded its current assets by \$9,124,847.46 at December 31, 2011, and \$8,495,858.15 at December 31, 2010. As discussed in Note 10, payments on the Company's loans have not been made as required. During the year ended December 31, 2010 the lenders accelerated and called due the note. No suit has been filed and the Company is in active negotiations to resolve this claim and is considering a variety of options. These factors create an uncertainty about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Note 9 - NOTES PAYABLE

Notes payable are as follows:

<u>Construction Phase</u>	<u>Original Loan</u>	<u>Date</u>	<u>Period</u>	<u>Interest Rate</u>
Phase I	\$ 3,463,000.00	11/28/1984	40 Years	7 1/2%
Phase II	3,000,000.00	03/11/1986	40 Years	6 5/8%

Note 9 - NOTES PAYABLE (Cont'd.)

	Outstanding Balance 2011	Outstanding Balance 2010
Amount FHA:		
Phase I	\$ 2,714,725.66	\$ 2,714,725.66
Phase II	<u>2,999,454.82</u>	<u>2,999,454.82</u>
Total Notes Payable	\$ 5,714,180.48	\$ 5,714,180.48
Less - portion due within one year	<u>3,824,430.82</u>	<u>3,445,360.18</u>
Total Long-Term Notes Payable	<u>\$ 1,889,749.66</u>	<u>\$ 2,268,820.30</u>

Interest expense for the years ended December 31, 2011 and 2010 was \$402,318.30 and \$402,706.94, respectively, none of which was capitalized.

Notes payable mature during the years ended December 31, in the following amounts:

Year	Principal Due
2012	\$ 3,824,430.82
2013	407,685.10
2014	438,465.47
2015	471,575.94
2016	507,193.51
Thereafter	<u>64,829.64</u>
Total	<u>\$ 5,714,180.48</u>

The original interest rate on the Phase I loan was 8 3/8%. According to P.L.-9998, the Water District was allowed to request the lower rate on (1) the date the loan was approved, or (2) the date the loan closed. This law was retroactive, when it became effective, so the Water District was eligible for the lower rate. Both loans allow for payment of interest only for the first two years with principal and interest payments commencing on the third anniversary date of the respective loans. Monthly payments will be \$25,246 per month for the Phase I loan, and \$18,030 per month for the Phase II loan. The payments on the Phase I and II notes have not been made as required by the original loan. The total accrued interest-unpaid, is reflected on the balance sheet.

Note 10 - SUBSEQUENT EVENTS

The District has evaluated events subsequent to the balance sheet date through February 10, 2012, and does not believe any events have occurred which effect the financial statements as presented.